(17)

No. 91-1513

In the Supreme Court of the United States

OCTOBER TERM, 1992

UNITED STATES DEPARTMENT OF THE TREASURY AND MITCHELL A. LEVINE, ASSISTANT COMMISSIONER, PETITIONERS

v.

GEORGE FABE, SUPERINTENDENT OF INSURANCE, STATE OF OHIO

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

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TABLE OF AUTHORITIES

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1. Respondent contends (Resp. Br. 8-10) that the plain language of the McCarran-Ferguson Act answers the question presented in this case. We agree. In our opening brief, we explain (Pet. Br. 14-16) that the Ohio priority statute does not regulate "the business of insurance" within the ordinary meaning of that phrase. The statute applies only when an insurer has been declared insolvent, its business has been wound up, and its assets are distributed among its creditors. The Ohio statute does not regulate the terms of insurance policies, the selling or advertising of insurance, or any other business activity of insurers. Thus, the Ohio statute plainly does not regu-

late the business of insurers, let alone "the business of insurance." [1]

Contrary to petitioner's contention (Resp. Br. 2), the Ohio legislature has not stated that payment of policyholder claims is the "paramount goal" of the liquidation process. Instead, the Ohio Code states that "the purpose of [the insurance insolvency laws] is the protection of the interests of insureds, claimants, creditors, and the public generally, with minimum interference with the normal prerogatives of the owners and managers of insurers, through * * * [e]quitable apportionment of any unavoidable loss." Ohio Rev. Code Ann. § 3903.02(D) (Anderson 1989). In accordance with that broader purpose, the Ohio priority statute ranks *all* types of claims against insolvent insurers. Concern for policyholders scarcely justifies subordinating claims of the United States to various *non-policyholder* claims, including claims of general unsecured creditors.

Moreover, the Ohio priority statute ranks two classes of claims—administrative claims and wage claims—*ahead* of policyholder claims. Thus, respondent's statement (Resp. Br. 17) that the Ohio priority statute "require[s] the insurer's assets to be applied first to full payment of losses under policies" is wrong. There is no guarantee that after the first two classes of claims have been paid, the remaining assets will be sufficient to pay policyholders' claims. Indeed, one commentator has noted that policyholder claims "are relegated to a relatively low status" and that

[1] The Ohio Code expressly distinguishes between "[r]egulation of the insurance business" and "[e]quitable apportionment of any unavoidable loss." Ohio Rev. Code Ann. § 3903.02(D)(4) and (6) (Anderson 1989 & Supp. 1991).

"[a]dministration expenses, and wage payments will often exhaust the insurer's assets." K. Doughty, *Policyholders' Rights in Insolvency Proceedings*, in *Law and Practice of Insurance Company Insolvency Revisited*, 1989 A.B.A. Tort and Ins. Practice Sec. 953, 975-976.

The Ohio priority statute contrasts sharply with other provisions of Ohio's insurance law that are intended to ensure that valid policyholder claims are paid. Ohio, like other States, has established an insurance guaranty fund to pay policyholder claims in the event the insurer becomes insolvent. See Ohio Rev. Code Ann. §§ 3955.01 *et seq.*, 3956.01 *et seq.* (Anderson 1989 & Supp. 1991). See generally National Conf. of Ins. Guaranty Funds Br. 1-3. The purpose of the guaranty fund is to pay covered policyholder claims without undue delay. *Id.* § 3955.03. Policyholder claims against insolvent insurers are paid out of the fund, and the fund is subrogated to the policyholder's claim against the insurer's estate. *Id.* § 3955.12(A). Consequently, the priority statute generally does not determine whether policyholder claims will be paid, but simply whether the guaranty fund or the federal government will bear the cost of unpaid claims of United States.[2]

Respondent errs in contending (Resp. Br. 2) that the Ohio priority statute regulates the business of insurance merely because it "is part and parcel of

[2] Ohio's guaranty funds cover most types of policyholder claims up to $300,000 without any deductible, *id.* Ohio Rev. Code Ann. § 3955.01 (Anderson 1989 & Supp. 1991) (or up to $100,000 for health insurance benefits, *id.* § 3956.04), including claims for refunds of unearned premiums. *Id.* § 3955.01.

a large, complex and specialized administrative system." See also Melahn Br. 7-9. This Court has recognized that "[m]any aspects of insurance companies are regulated by state law, but are not the 'business of insurance,'" including "the composition of their boards of directors, when their books and records could be inspected, how they could invest their funds, [and] when they could liquidate or merge." *Group Life & Health Ins. Co.* v. *Royal Drug Co.*, 440 U.S. 205, 230 n.38 (1979). Similarly, respondent contends (Resp. Br. 9) that "the liquidator of an insolvent insurance company performs all functions necessary to conduct the business of insurance," and therefore engages in "the business of insurance" for purposes of McCarran-Ferguson. That responds to an argument we have not made. We do not contend that *no* statute regulating insurance company liquidators may be a regulation of "the business of insurance," but merely that the Ohio priority statute at issue here is not such a regulation.[3]

2. Some of respondent's amici contend that this Court's three-part test for determining whether a practice is part of "the business of insurance," see *Union Labor Life Ins. Co.* v. *Pireno*, 458 U.S. 119, 129 (1982), applies only in the antitrust context.

[3] Respondent and some of his amici rely on cases in which federal courts have abstained from deciding issues connected with insurer insolvencies on the basis of *Burford* v. *Sun Oil Co.*, 319 U.S. 315 (1943). See Resp. Br. 5 n.3; Gordon Br. 20-22; Melahn Br. 11-13. Although the existence of a comprehensive state system of insurance regulation may support *Burford* abstention in appropriate cases, it does not follow that every state law that regulates insurance companies is a law regulating "the business of insurance" for purposes of McCarran-Ferguson.

The amici contend that a different—and much less rigorous—test applies elsewhere. See Mich. Br. 22-47; Va. Bureau of Ins. Br. 18-21; Curiale Br. 11-15; Selcke Br. 26-27; Council of State Gov'ts Br. 22-27; NAIC Br. 11-13. Respondent himself rejects this radical argument, see Resp. Br. 15 n.18—and for good reason.

Section 2(b) of the McCarran-Ferguson Act provides, in part:

> No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating *the business of insurance*, unless such Act specifically relates to *the business of insurance: Provided*, That * * * [the federal antitrust statutes] shall be applicable to *the business of insurance* to the extent that such business is not regulated by State Law."

15 U.S.C. 1012(b) (emphasis added). Congress thus used the identical phrase "the business of insurance" in consecutive sentences of a single subsection of McCarran-Ferguson. The "normal rule of statutory construction" is that "identical words used in different parts of the same act are intended to have the same meaning." *Sullivan* v. *Stroop*, 496 U.S. 478, 484 (1990), quoting *Sorenson* v. *Secretary of the Treasury*, 475 U.S. 851, 860 (1986), quoting *Helvering* v. *Stockholms Enskilda Bank*, 293 U.S. 84, 87 (1934), quoting *Atlantic Cleaners & Dyers, Inc.* v. *United States*, 286 U.S. 427, 433 (1932). There is no reason to depart from that rule in this case. Indeed, the "normal rule" applies with added force where the

same words are used more than once in a single subsection of a statute.[4]

In support of their contention that Congress intended that the phrase "business of insurance" have one meaning in antitrust cases and another meaning in other cases, the amici observe that both *Pireno* and *Royal Drug* involved alleged violations of the antitrust laws. Respondents ignore the *Pireno* and *Royal Drug* pedigree. The test the Court applied in those cases incorporated and refined the Court's analysis in earlier *non-antitrust* cases. For example, the requirement of risk transfer is derived directly from *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U.S. 65 (1959). See *Royal Drug*, 440 U.S. at 212. And the requirement that "the practice is an integral part of the policy relationship between the insurer and the insured," *Pireno*, 458 U.S. at 129, is a refinement of the Court's analysis in *SEC* v. *National Securities Inc.*, 393 U.S. 453, 460 (1969). The suggestion that the *Pireno* test applies only in antitrust cases is also refuted by this Court's decisions employing the *Pireno* test to construe similar language in ERISA. See *Pilot Life Ins. Co.* v. *Dedeaux*, 481 U.S.

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[4] Amici derive their proposal largely from Howard, *Uncle Sam Versus the Insurance Commissioners: A Multi-Level Approach to Defining the "Business of Inurance" Under the McCarran-Ferguson Act*, 25 Willamette L. Rev. 1 (1989). The author of that article frankly recognizes that "a dual definition would contravene the principle * * * that the same words used in close proximity within the same statute should have the same meaning," and would imply "that the Congress that passed the McCarran Act was extraordinarily inept in its draftsmanship abilities." *Id.* at 39 n.114.

41, 48-49 (1987); *Metropolitan Life Ins. Co.* v. *Massachusetts*, 471 U.S. 724, 743 (1985).[5]

The amici correctly note that Section 2(b) has dual purposes:

> [T]he *primary* purpose of the McCarran-Ferguson Act was to preserve state regulation of the activities of insurance companies, as it existed before the *South-Eastern Underwriters* case. * * * The McCarran-Ferguson Act operates to assure that the States are free to regulate insurance companies without fear of Commerce Clause attack. * * * [T]he quite different *secondary* purpose of the McCarran-Ferguson Act [is] to give insurance companies only a limited exemption from the antitrust laws.

Royal Drug, 440 U.S. at 218 n.18. Congress created a limited antitrust exemption for insurer activities that are (1) part of "the business of insurance," (2) regulated by state law, and (3) not acts of boycott, coercion or intimidation, 15 U.S.C. 1013(b). *Pireno*'s relatively narrow construction of "the business of insurance" advances this congressional purpose and is consistent with the rule that "exemptions from the antitrust laws must be construed narrowly." *Pireno*, 458 U.S. at 126; see also *Royal Drug*, 440 U.S. at 231.

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[5] Amici suggest (Mich. Br. 40-41) that *Pireno* and *Royal Drug* are inapposite because those cases examined particular practices of insurers, while this case concerns a state statute. But in determining whether a state statute regulates "the business of insurance," it is necessary to consider the practices that are regulated by the statute. In this case, *no* business practice of insurers is at issue, because the insolvent insurer's business affairs have been wound up.

Contrary to amici's contention, *Pireno*'s construction of "the business of insurance" preserves the States' traditional authority to regulate the activities of insurers. In the decade since the Court's decision in *Pireno*, we are aware of no decision invalidating a state law regulating insurance companies on Commerce Clause grounds. The *Pireno* test thus is fully adequate to "assure that the States are free to regulate insurance companies without fear of Commerce Clause attack." *Royal Drug*, 440 U.S. at 218 n.18.[6]

3. In contrast to his amici, respondent acknowledges (Resp. Br. 15 n.18) that the *Pireno* test applies in this case. Respondent's contention (*id.* at 17) that the Ohio priority statute "meets all three *Pireno* criteria" is unpersuasive.

a. In our opening brief, we explain (Pet. Br. 16-19) that the first *Pireno* factor—whether the practice at issue "has the effect of transferring or spreading a policyholder's risk," 458 U.S. at 129—requires, at a minimum, that the insurer undertake some risk. The Ohio priority statute does not involve a transfer of risk from the policyholder to the insurer. The statute simply determines the order in which creditors of an insurance company will be paid in the

[6] In place of the *Pireno* test, the amici urge the Court to apply a less demanding test that they extract from this Court's decision in *SEC* v. *National Securities*, *supra*. As we explain below, see pp. 10-11, *infra*, the Ohio priority statute does not regulate "the business of insurance" as that phrase was construed in *National Securities*. The Ohio statute has nothing to do with the validity of a policyholder's contractual claim, and does not "so closely affect the 'reliability, interpretation, and enforcement' of the insurance contract * * * as to fall within the exempted area." *Royal Drug*, 440 U.S. at 216. See *Idaho ex rel. Soward* v. *United States*, 858 F.2d 445, 452-453 (9th Cir. 1988).

event the insurer becomes insolvent. Nor does the Ohio statute involve risk spreading—*i.e.*, the assumption of numerous, relatively small, independent risks that occur randomly over time. Each of the insurer's policyholders (as well as the insurer's other creditors) faces the identical risk that the insurer will become insolvent. Thus, the creditors do not face numerous, independent risks of insurer insolvency.

Respondent contends (Resp. Br. 17) that "the risk is not spread until insurer assets are used to pay a covered loss." See also *id.* at 18 (denying that "the transfer of risk is complete at the time the insurance policy is issued"). This Court has squarely rejected petitioner's contention. In *Pireno*, the insurance company argued that "the transfer of risk from an insured to his insurer actually takes place not when the contract between those parties is completed, but rather only when the insured's claim is settled." 458 U.S. at 131. The Court concluded that "[t]he transfer of risk from insured to insurer is effected by means of the contract between the parties—the insurance policy—and that transfer is complete at the time that the contract is entered." 458 U.S. at 130. That principle applies in this case and refutes respondent's argument that the Ohio priority statute transfers risk.[7]

[7] Respondent's contention (Resp. Br. 17) that "claims adjustment is part and parcel of the 'business of insurance' " is beside the point. The Ohio priority statute does not regulate the process of determining the validity and amount of a policyholder's claim. Instead, the statute simply determines the order in which valid claims—including policyholder claims—will be paid out of the estate of an insolvent insurer. Cf. *Pireno*, 458 U.S. at 138 n.3 (Rehnquist, J., dissenting) (noting difference between "method of paying a claim" and "more fundamental process of assessing the validity of a claim and determining the amount to be paid").

b. Respondent contends (Resp. Br. 19) that the second *Pireno* criterion—whether the practice is "an integral part of the policy relationship between the insurer and the insured," 458 U.S. at 129—is satisfied because the Ohio priority statute increases the probability that a policyholder's claims will be paid. But the Ohio priority statute, rather than addressing the relationship between policyholder and insurer, addresses the relationship among the various classes of creditors of the defunct insurer. As we explain in our opening brief (Pet. Br. 19-20), the Ohio priority statute has nothing whatever to do with the validity or amount of the policyholder's contractual claim against the insurer. Instead, the statute comes into play only if (1) it is determined, under other provisions of law, that the policyholder has a valid claim against the insurer, and (2) the insurer becomes insolvent and is liquidated. At that point, the insurer's business has been wound up, and there is no continuing relationship between the policyholder and the insurer.

Nor does the Ohio priority statute "so closely affect the 'reliability, interpretation, and enforcement' of the insurance contract * * * as to fall within the exempted area." *Royal Drug*, 440 U.S. at 216. As we have explained, see p. 3, *supra*, Ohio has established an insurance guaranty fund to pay valid policyholder claims against insolvent insurance companies. See Ohio Rev. Code Ann. §§ 3955.01 *et seq.* (Anderson 1989 & Supp. 1991), 3956.01 *et seq.* (Anderson Supp. 1991). Because the priority statute is unlikely to determine *whether* a policyholder's claim is paid, it is not so closely connected to the contractual relationship between the insurer and the insured as to qualify for the McCarran-Ferguson exemption.

Pireno, 458 U.S. at 132. It is true that according priority to federal claims may increase demands on state insurance guaranty funds, and that in turn may increase the insurers' cost of doing business. But as the Court recognized in *Royal Drug*, virtually all state regulation of insurance companies has some effect on the insurance companies' cost of doing business. An argument that such an effect is enough to bring the statute within the McCarran-Ferguson exemption thus "proves too much." 440 U.S. at 216.

c. Respondent argues (Resp. Br. 19-20) that the Ohio priority statute is "limited to entities within the insurance industry," 458 U.S. at 129—the third *Pireno* factor—because it applies to insurance companies. The Ohio statute plainly is not *limited* to entities within the insurance industry. The statute regulates the priority of *all* types of creditors' claims against insolvent insurers, including many creditors that are not part of the insurance industry. Although respondent characterizes non-policyholder claims as "tangential," Resp. Br. 20, the Ohio priority statute itself ranks two classes of non-policyholder claims ahead of policyholder claims.

Respondent's proposed redefinition of the third *Pireno* factor to cover any group of entities that *includes* insurance companies would expand the "business of insurance" beyond any manageable limits. Respondent's approach is also inconsistent with the purpose of this factor, which is to reflect "the primary concern of both representatives of the insurance industry and the Congress * * * that cooperative rate-making efforts be exempt from the antitrust laws." *Royal Drug*, 440 U.S. at 221.

4. Respondent contends (Resp. Br. 20-26) that the enactment history of McCarran-Ferguson sup-

ports the view that the Ohio priority statute regulates the "business of insurance." Respondent is incorrect. Congress enacted McCarran-Ferguson in the wake of *United States* v. *South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), which held that "the business of insurance is interstate commerce." *Royal Drug*, 440 U.S. at 217. The Act was intended to assure that state regulation and taxation of the business of insurance would not be found to violate the Commerce Clause. See *Royal Drug*, 440 U.S. at 218 n.16 (quoting S. Rep. No. 20, 79th Cong., 1st Sess. 1-2 (1945); H.R. Rep. No. 143, 79th Cong., 1st Sess. 2 (1945)). Because the Act was largely "an attempt to turn back the clock" to the days prior to the Court's decision in *South-Eastern Underwriters*, *National Securities*, 393 U.S. at 459, Congress did not intend "to clothe the States with any power to regulate or tax the business of insurance beyond that which they had been held to possess prior to" that decision, H.R. Rep. No. 143, *supra*, at 3.[8]

Prior to the decision in *South-Eastern Underwriters*, it was clear that States had no power to override the federal priority statute in insurance insolvency proceedings. That is so because the federal priority statute does not rest on Congress's power under the Commerce Clause, but instead on its power "[t]o establish * * * uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. Art. I, § 8, Cl. 4. It is therefore not surprising that

[8] McCarran-Ferguson did not "turn back the clock" in all respects because it did not grant the States all the regulatory authority that they possessed prior to *South-Eastern Underwriters*. But Congress did not grant the States any *additional* authority beyond the authority that they had traditionally possessed. See Pet. Br. 23-25 & n.10.

this Court held, prior to *South-Eastern Underwriters*, that the federal priority statute applied in state proceedings to liquidate an insolvent insurance company and preempted an inconsistent state statute. *United States* v. *Knott*, 298 U.S. 544 (1936).

Respondent's efforts to distinguish *Knott* are unconvincing. Respondent asserts (Resp. Br. 26) that "[n]owhere in the Florida statutes are priorities to special deposit funds established," and that consequently "[n]o state priority statute was pre-empted or impaired when this Court determined that the bond claims of the federal government were entitled to priority." Respondent is simply incorrect. The Florida statute at issue in *Knott* plainly provided for payment of in-state creditors ahead of all other creditors. See 298 U.S. at 546. Although the Ohio priority statute contains a more elaborate classification of claims, the statute at issue in *Knott* unquestionably was a form of priority statute—it ranked claims of Florida creditors ahead of other claims.

Respondent also observes (Resp. Br. 26) that *Knott* involved the disposition of assets that an out-of-state insurer placed on deposit with Florida as a condition of doing business in that State. But nothing in the Court's opinion suggests that it would have reached a different result if some other type of insurance company asset had been at issue. If anything, the nature of the assets at issue in *Knott* suggests that the State had a heightened interest in controlling their disposition.[9]

[9] State courts, both before and after McCarran-Ferguson, reached the same result as this Court in *Knott*. See Pet. Br. 24 n.11 (collecting authorities). Respondent asserts (Resp. Br. 25) that, prior to *South-Eastern Underwriters*, courts

5. Finally, respondent and his amici contend, as a matter of policy, that claims of the United States should not be entitled to first priority in insurance insolvency proceedings. The short answer is that these arguments should be addressed to Congress, not the courts. In any event, respondent's policy arguments are overstated.

The purpose of the federal priority statute is to "secure an adequate revenue to sustain the public burdens, and discharge the public debts." *United States* v. *State Bank*, 31 U.S. (6 Pet.) 29, 35 (1832). According first priority to federal claims thus advances the strong public interest in increasing the federal revenue and reducing the deficit.

Respondents' amici assert that the federal interest in deficit reduction is more than offset by the States' interest in protecting policyholders against loss in the event of insurer insolvency. See NAIC Br. 14 ("States would be rendered incapable of providing the special protection needed by policyholders."). But as we have explained, see p. 3, *supra*, policyholder claims against insolvent insurance companies generally are paid out of insurance guaranty funds, which are then subrogated to the policyholders' claims

held that "where a state had specifically legislated the priority of claims, the federal priority statute would not supersede the clear state legislative intent." The single authority that respondent cites, *Conway* v. *Imperial Life Ins. Co.*, 21 So. 2d 151 (La. 1945), does not support that proposition. In *Conway*, the court held that the federal priority statute did not apply because the assets at issue were held "in trust * * * as security for the policy holders," and therefore were not part of the insurance company's estate. *Id.* at 154. See *Knott*, 298 U.S. at 548 (federal priority statute inapplicable if state statute divests insurance company of title to assets).

against the insurer's estate. According first priority to federal claims may increase the demands on guaranty funds, and that in turn may increase the insurers' cost of doing business. But the alternative is to leave valid claims of the United States unsatisfied —a loss ultimately borne by the citizens of all the States.

Respondents' amici also suggest (Selcke Br. 8) that applying the federal priority statute will "wreak havoc" on state regulation of insurance companies. That concern is greately overstated. Resolution of the narrow question presented in this case—whether claims of the United States are entitled to first priority in insurance insolvency proceedings—will not call into question the States' broad authority to tax and regulate the business of insurance.[10]

[10] Amicus National Conference of Insurance Legislators contends (Br. 5-20) that the federal Bankruptcy Code, McCarran-Ferguson, and the federal priority statute, when read together, demonstrate that Congress did not intend the federal priority statute to apply in insurance insolvency proceedings. That contention is wholly unconvincing. The federal Bankruptcy Code does not apply to insurance companies. See 11 U.S.C. 109(b)(2), 109(d). Consequently, the provisions of the Bankruptcy Code establishing the priority of claims of the United States do not affect "the priority of claims of the United States in non-bankruptcy proceedings." *United States* v. *Emory*, 314 U.S. 423, 427 (1941). When Congress amended the federal priority statute in 1978 to make clear that it does not apply in proceedings under the federal Bankruptcy Code, Congress did not state or imply that the priority statute would no longer apply in non-bankruptcy proceedings. Act of Nov. 6, 1978, Pub. L. No. 95-598, § 322(a), 92 Stat. 2678.

For the foregoing reasons and those stated in our opening brief, the judgment of the court of appeals should be reversed.

Respectfully submitted.

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